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The recent Cuban crisis has forcefully brought to the attention of United States citizens the grassroots revolution which is taking place in the Latin American countries. Social, economic and political cataclysms are currently turning many of the twenty independent republics to radical solutions similar to the history of Czarist Russia in the period just prior to the Bolshevik uprisings.[1] Although the United States has been attempting to stem this powerful tide towards Communism through its twenty-billion-dollar aid program from the Alliance for Progress, the results have only been minimal. The population of these countries continues to explode with an estimated five hundred million inhabitants projected for the year 2000.[2]

Despite the efforts of Dr. Raul Prebisch and the United Nations Economic Commission for Latin America (ECLA),[3] the economic relations between Latin America and the European Common Market continue to weaken instead of strengthen.[4] Political institutions remain unstable and the masses are still impoverished. Bloody revolts rock Venezuela and Colombia, the military use tanks to stage coups in Buenos Aires and Lima, women riot in Rio de Janiero over food shortages, and guerillas maneuver in the hills of Guatemala. In many of the places, the social, economic and political changes cannot be measured accurately since statistics are collectible only in highly developed countries. The simple annals of a village of Guatemala or a mining town in Bolivia are not easy to locate, but the basic changes taking place cannot be mistaken.[5] We are becoming more

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[1] Latin America, Business Week, September 22, 1962, p. 158.

[2] Benham & Holley, A Short Introduction to the Economy of Latin Americas (1960).

[3] Hirschman, Latin American Issues—Essays and Comments, 12-29 (1960).

[4] *Latin America and the European Common Market*, 1963 Atlas 40.

[5] For the outstanding current works on the social, economic and political changes in Latin Americas see Tannenbaum, Ten Keys to Latin America (1962); Porter and Alexander, The Struggle for Democracy in Latin America (1961); de Madariaga, Latin America Between the Eagle and the Bear (1962); Social Change in Latin America Today (1961); Alexander, Today's Latin America (1962); Berle, Latin America—Diplomacy and Reality (1962).

conscious of the fact that we are living in the shadow of a volcano that might erupt at any time.[6] We are also aware of the need to find some means of better understanding those Latin American forces which will influence our destiny much more in the future than they ever have in the past.

It is hard to generalize about the twenty Latin American economies.[7] Venezuela probably enjoys ten times the per capita income of hard-pressed Bolivia, and modernized Mexico appears to be growing at a good rate while other countries are not even growing. The political pattern is also complex and has a tremendous impact on Latin American economic life. Mexico, for example, is autocratically ruled by a single party. Feudal and monied aristocracies are powerful in Peru, Ecuador and elsewhere. Dictatorships smother potential opposition in Nicaragua, the Dominican Republic and Paraguay—and now in Cuba.[8]

Latin America is coming into industrialization at a time when technology elsewhere is already in an advanced state, and is torn between choosing the Soviet method of economic development[9] or the free-enterprise, free-market system countered by the United States laissez faire capitalistic system. The normal Latin American cultural tendency is to be statist while the Anglo American tradition includes the element of individual responsibility.[10] A governmental function in all Latin American countries has been the promotion of industrialization, and because Latin American credit has usually required the government guarantees for external business development loans, it has necessarily become involved in the industrialization process.[11]

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[6] National Observer, January 7, 1963, p. 22.

[7] Former Senator William Benton, in his travels with Adlai Stevenson, found that the voice of Latin America had many accents. Benton, the Voice of Latin America (1961). In his excellent analysis of Latin America, Senator Benton said, "These countries do not speak with a single voice. They have voices which make up a chorus, often harmonious but sometimes discordant. To think of them as a unit—or to treat them as if they were a single nation or a single people—invites grave misunderstanding and confusion."

[8] While the Dominican Republic has at long last rid itself of Trujillo, it is still too early to know in which direction the new regime will travel. National Observer, December 24, 1962, p. 3, col. 4.

[9] Dozer, Are We Good Neighbors? 310 (1959).

[10] Burck, *Latin America: Bureaucracy or the Market?* Fortune, February 1962, p. 86.

[11] A discussion of the responsibility and the role of American private initiative in Latin America is contained in Bohan, *Private vs. Public Economic Initiative in Development of Latin America*, 2 Institute on Private Investment Abroad 121 (1960).

There is a shortage of capital in Latin America and one sign of this is the high rates of interest prevailing throughout the area.[12] As a general rule, banks are pressing against the legal ceilings on interest rates, and they are usually finding ways of circumventing them. Bank lending rates are generally limited to a maximum of around twelve per cent a year, but commissions and other hidden charges often push the actual cost up to as much as eighteen per cent. In Brazil, businessmen complain that bank officials frequently ask for a participation in the enterprise as a condition for granting credit. Even so, the banks are unable to meet the heavy demand for loans because of the inadequacy of their resources.

What is more, the banks in most Latin American countries have found that they can get around the interest rate limitations on both deposits and loans by setting up "financieras."[13] These are finance companies which may sell shares or accept savings deposits, issue bonds or borrow funds, and re-lend at rates of interest much higher than the banks are permitted to charge. For example, in Brazil where the legal ceiling for bank loans is twelve per cent, the financieras lend against good commercial paper at rates up to forty per cent a year.[14] In Argentina, the banks are limited up to fifteen per cent, but their financieras also charge up to forty per cent. They pay eighteen per cent on their shares or borrowings.[15] In Mexico, where inflation and devaluation have been less of a problem, the financieras charge fifteen to twenty-two per cent a year. Their bonds, which they redeem at par on sight, yield eight per cent a year.[16]

The high cost of money in these countries seems to have little to do with the policies currently pursued by the central banking authorities.[17] Some of the central banks are ostensibly employing

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[12] *A U.S. Company in a Latin Squeeze,* Fortune, February 1962, p. 218.

[13] Ellis and Wallich, Economic Development for Latin America, proceedings of a conference held by the International Economic Association, 171-175 (1961).

[14] For an excellent article which deals fully, factually and fairly with the prerevolutionary condition in which Brazil currently finds itself, written by a European correspondent, see Singer, *Brazil Stands on the Brink,* 1962 Atlas 349.

[15] National Observer, January 7, 1963, p. 22.

[16] For a brief survey of taxation and the law in investment in Mexico, see Brudno, *Tax and Legal Aspects of Investment in Mexico,* 2 Institute on Private Investments Abroad 403 (1960). For a more exhaustive treatment, see Gumpel & Margain, Taxation in Mexico (1957), another text of the World Tax Series published by the Harvard Law School's program on international taxation.

[17] Stark, Social and Economic Frontiers in Latin America 56 (1961).

very restrictive policies; others are exercising virtually no control over credit. The only country where money is not extremely expensive and where banks can fully meet loan demands is in Panama, where there is no central bank. Panama,[18] which uses the United States dollar for its currency and has one of the hardest monies in the Latin American area, is the only country that has a relatively reasonable structure of interest rates.

While interest rates of up to forty per cent in Argentina may appear very attractive to lenders at first glance, when one finds that the value of the Argentine peso has been nearly halved since last March, interest to invest in Latin America soon wanes and is one of the causes of the capital shortage. Inflation, past and present, is certainly a major factor.[19] Some of the Latin American countries are taking measures to curb inflation—but once confidence in a currency has been severely shaken, it is not easy to restore. It takes confidence to encourage savings, and to get capital to flow into a country and stay there. The United States, in order to assist, has agreed to make available a ninety-day credit of 30 million dollars to Brazil, the government having pledged to prepare "definite plans and measures for putting into force, beginning early 1963, an effective program to limit inflationary pressures as well as a development plan designed to support strong and balanced economic growth."[20]

The cruzeiro, the Brazilian basic currency unit, sold for some 200 to the dollar two years ago; now it is quoted as high as 1,000 to the dollar. The cost of living rose some sixty per cent in 1962 alone. To pay off deficits and loans, the government keeps issuing more money. More money in circulation means the money is worth less, so workers get a pay raise to keep pace and prices keep going up. Foreign investment, which could provide a new source of money, has almost stopped because the economic climate is so shaky.[21] New United States investment in Brazil, for instance, has dropped in two years from 100,000,000 dollars annually to almost nothing.

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[18] The monetary unit of Panama is the balboa and is equivalent to the United States dollar.

[19] See the essay by Roberto de Oliviera Campos, *Two Views on Inflation in Latin America*, Hirschman, *op. cit. supra* note 3, at 69.

[20] Wall Street Journal, Tuesday, January 8, 1963, p. 9, col. 1.

[21] See the study by Charles Wagley, Social Change in Latin America 177-230 (1960). National Observer, January 7, 1963, p. 1, col. 4.

The United States business investor is operating in Latin America today in a climate of agitation against foreign capital and, more and more, against the system of private enterprise itself.[22] Hostility to foreign capital comes not only from the Communists but also from the rightwing nationalists and local businessmen. In Brazil, a leading industrialist subsidized a Communist campaign—including student demonstrations—against American Can Company when it proposed to open a new plant. When the British-American Tobacco Company contemplated establishing a plant in Colombia, opposition by the tobacco monopoly kept machinery standing on the docks in England for two years and finally killed the project.

In Brazil, the feeling against foreign capital and in favor of government intervention in the economy runs highest.[23] State governments have seized several United States-owned utilities, and the central government is now negotiating a take-over of all foreign-owned utilities valued at more than one billion dollars. The mines ministry has virtually halted new foreign mining development and takeovers are threatened in telecommunications and air transport.

Despite these risks, United States investment will continue to flow into some parts of Latin America this year because the area is a growing market, with a pent-up demand for some products.[24] To meet unsatisfied demands for automobiles, for example, auto makers in Brazil are plowing back profits to expand production. In Argentina, the bulk of an expected 308 million dollars in foreign investment will go into automobile plants, protected from outside competition by import restrictions, and selling locally produced compacts at sky-high prices of 5,000 dollars or more. The United Nations Economic Commission for Latin America

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22 One could detail this in a thousand ways from the cocktail to baseball, from the American movie to the Cadillac, from frozen orange juice to nail polish, from Coca Cola to the office secretary, and from the American advertisement on television to the lilting jazz played by the orchestra in the "best" restaurants. The Mexicans have invented a word for it—*pochismo*, the substitute of the foreign, especially the American, for local traditional Mexican or Spanish usage, belief, or attitude. Tannenbaum, Ten Keys to Latin America 174-175 (1962).

23 Palmer, Search for a Latin American Policy, 189-202 (1957).

24 Professor Gomez, of the Law Institute of the Americas, The Southwestern Legal Center, Dallas, Texas, has prepared a survey of Latin American Business Associations for the benefit of American investors. 1 Institute on Private Investments Abroad 337 (1959).

(ECLA) puts the combined Latin American market for autos at 1.8 million vehicles a year by 1975.

As a result of greater public interest in such Latin American investment possibilities, and encouraged by the approval of the representatives of the Organization of American States seeking programs for social improvement and economic development, tax reform has been assigned an especially high priority on the agenda of surveys and studies to be undertaken and of objectives to be achieved.[25] In furtherance of the Act of Bogota (Doc. CECE/III 70; approved by Council of OAS, Oct. 11, 1960), governments of the member states have created and capitalized the Inter-American Development Bank,[26] and it is anticipated that the Bank's promotion of development will be supplemented by increased investment and activity of United States enterprises in lands south of the border.

A discussion of the taxation of United States investments in Latin America involves consideration of United States tax law and of the tax systems of twenty independent republics. Rather than discuss the tax system of each of the Latin American nations, some of which have as many as 200 separate taxes in effect, this paper will first delineate briefly the Brazilian[27] and Colombian[28] tax systems, and compare certain features of these two systems with those in other countries. Simultaneously, some important provisions of the United States Internal Revenue Code applicable to income earned abroad will be reviewed.[29]

Except for some tax specialists and the accounting departments of business enterprises which are already operating in Latin America, there is little knowledge in our country about the

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[25] Crockett, *Tax Patterns in Latin America,* 15 Nat'l Tax J. 93 (1962).

[26] The Inter-American Development Bank, with Felipe Herrara of Chile as director, came into legal existence January 1, 1960, with a capital of $850 million. The United States subscription is in the amount of $450 million. It has been clearly stated that the bank is intended to constitute an addition to, not just to replace, existing sources of development funds for Latin America.

[27] For the outstanding and most complete coverage of Brazilian taxation, see Gumpel and De Sousa, Taxation in Brazil (1957). This text is one of a series published by the Harvard Law School through its World Tax Series which is included in its International Program in Taxation.

[28] Pomerantz, *Taxation of United States Investments in Latin America,* 44 Va. L. Rev. 205 (1958); Cavelier, A Statement of the Laws of Colombia (1963).

[29] The Internal Revenue Code of 1954, as amended by some new rules in 1962, spells out in subchapter *N* how the United States will tax income from sources within or without the United States.

tax systems of the twenty southern republics.[30] We have tended to be provincial about taxation manifested by references to "income," as if the cocept were international, and tying it in a Siamese twin fashion to "taxation." At the same time we have used "rate scales" as if the progression were a fair index for a comparison of tax burdens. Generally, we do not realize that most other nations derive their greatest revenues from customs duties and from sales, production and stamp taxes. Many of the more developed Latin American republics did not adopt income taxation until the 1930's.[31] The full picture becomes more complicated by the evolving nature of Latin American taxes, often without the intervening or transitional administrative experience which leads to or develops precise definitions and concepts.

What kinds of taxation make up a Latin American tax system? After a Latin American government received its independence, it would rely overwhelmingly on indirect taxation. The principal taxes were import duties, taxes on sales, consumption and production. The government would also impose a tax on legal documents and official acts. Such taxes were usually collected by the use of stamps or stamped paper. Taxes were also imposed on land for which the taxable base was sometimes not the land's fair market value. More often than not, a theoretical annual rental value was imputed to such real estate.[32]

Colombia, like many of her sister republics, has a mass of uncodified tax legislation. Characteristic of Latin American tax legislation is a relative vagueness, and one longs for voluminous regulations and the Internal Revenue Bulletin, but they just do not exist.[33] The income tax of many of the republics must be

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[30] Several U.S. accounting firms and banks operating in Latin America publish pamphlets for their clients and prospective clients, which describe the forms of doing business in these countries and the various local taxes and other business problems. See Powell, *Some Legal and Practical Problems Encountered by U. S. Concerns Performing Services in Latin America*, 4 Institute on Private Investments Abroad 25 (1962).

[31] Pomerantz, *supra* note 28, at 205.

[32] The Latin American elite had been given *fueros* by the Spanish monarchs during the colonial period which included exemption from taxation. For the current problems of the Latin American elite, see Nunez, *The Importance of the Latin American Elite*, Fortune, January 1963, p. 70.

[33] The Foreign Tax Law Association has attempted to provide a loose-leaf service for many of the Latin American countries, but its efforts to date have not been very satisfying. In addition, the Pan American Union has also published the laws of these countries, but only one chapter in each of the translated compendiums deals specifically with taxation.

sought in a vast mass of laws, decrees, decree-laws, proclamations, ministerial decrees and other forms of legislation which are usually brief in scope, and which create new taxes, or amend, modify or repeal all or parts of prior legislation which often is not cited. There is a lack of precision and detail in legislation and regulations with the result that much must often be inferred. As an example, although business expenses are deductible and are defined as those required for the production of income,[34] under recognized accounting principles, the rules will then proceed to place a limitation on such a deduction for salaries paid to managers or disallowing all expenses that may be incurred abroad.

If one were to look for a reason for this very frustrating lack of detail, the tax historian would find that the ancient Commercial Codes helped to create the present system which only requires a prescribed set of books to be maintained and registered in the city within which the business operates.[35] The entries reflect all of the local business transactions and the government wisely refuses to disturb the established customs. If the owner or his bookkeeper have evolved an accounting system that satisfied them,[36] and these accounting schemes differ greatly, the Latin American revenue agent will accept it, despite his complaints that the records are difficult to interpret.

Colombian income taxation consists of six separate taxes,[37] while among the Brazilian taxes which are of particular importance for the foreign investor or businessman are the income tax and excess profits tax, the federal excise or "consumption" tax, and the customs tariff (which recently has been completely revised).[38] Of the six Colombian income taxes, only four apply to United States citizens and their investments in the country.

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[34] Gibbons, Tax Factors in Basing International Business Abroad—a Study of the Law of the United States and Selected Foreign Countries, Harvard Law School International Program in Taxation (1957).

[35] An explanation of the recent evolution of the concept of free trade in Latin American integration in general is contained in Urquidi, Free Trade and Economic Integration in Latin America (1962). See also the papers of the 29th Couchiching Conference, The Latin Americas (1960).

[36] In the United States, the Commissioner of Internal Revenue will ordinarily permit different methods of accounting provided they adequately reflect income. See subchapter E on Accounting Periods and Methods of Accounting, Int. Rev. Code of 1954 §§ 441-462.

[37] Pomerantz, *Taxation of United States Investments in Latin America*, 44 Va. L. Rev. 206 (1958).

[38] The Taxation of Business Income from Foreign Operations 110-121 (1958).

One of these is not a tax on income but is rather a tax on "patrimony" of the taxpayer, or, as we would term it, on his net assets, and the rate is only one and one-half per cent.[39] Two reasons can be offered as to why Colombians insist on calling the patrimony tax an income tax. The first is that it is a sort of "reverse" income tax which penalizes those who hold valuable assets, principally land, without using them to produce taxable income. The second reason is that the net assets tax computation results in a basis for the excess profits tax. Under the Colombian system, taxable excess profits are deemed to exist when the net income of the taxpayer exceeds twelve per cent of his net assets as computed for the patrimony tax. These excess profits are taxed on a graduated scale ranging up to fifty-one and one-quarter per cent.[40]

The taxes of Brazil are fairly typical in most respects of the Latin American systems, and can well illustrate the differences between those systems and the methods of taxation prevailing in the United States.[41] Brazil is divided politically into twenty-one states, five territories and a federal district. These are subdivided into about three thousand townships or municipios.[42] The federal, state, and municipal governments impose and collect taxes, and for 1960 the Federal Government took forty-five per cent of all revenues, which aggregated nearly 180 billion cruzieros, of which ninty-five per cent represented tax receipts. Of these tax receipts, about forty per cent was derived from consumption taxes; thirty-five and one-half per cent from income taxes; thirteen and one-third per cent from stamps and other internal taxes; and, exceptionally for Latin America, only eleven and one-tenth per cent from duties on imports.

The Brazilian state governments which receive forty-four per cent of total public revenues, derived seventy-seven per cent from taxes, the principal ones being on sales (about seventy per cent of the total). Other taxes are on suburban and rural

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[39] In Lanham & Kemp-Barclay & Co. of Colombia v. Commissioner, 26 T.C. 582 (1956), the United States would not permit a foreign tax credit for a "patrimony" tax but only for an income, or in lieu of income, tax.

[40] These rates were established by decree 0270 of February 6, 1953, art. 32 (*Diario Oficial* of Feb. 25 and March 9, 1953).

[41] For a general discussion of taxation of foreign income, see Bittker and Erb, Taxation on Foreign Income (1960).

[42] Gumpel and De Sousa, *op. cit. supra* note 27, at 7.

land, transfers of land and inheritances. There are also stamp taxes in Brazil.[43] The remaining eleven per cent of public revenues is the share going to the municipal governments, and they are chiefly on urban real estate and rents. The municipos also impose taxes on business and professional activities, admissions to shows and some stamp taxes. There is a substantial variation existing in both state and local tax patterns.

Generally, Brazilian taxes apply to all of the goods that are produced, imported or sold within its borders.[44] Jurisdiction to tax is also extended by Brazil to transactions and activities which are carried out within its territory, and to land and other property situated therein. Taxation in Brazil and the other Latin American countries usually ends at the frontier. There are some exceptions to this principle,[45] but ordinarily the taxable property must be physically within reach of the taxing authority. For any activities to be taxed, they must be locally conducted.

The source of income rules indicate that taxation is limited to domestic, as distinguished from foreign source income, although at present the laws of some Latin American republics subject to tax income derived from any source in the world by their citizens, residents and companies—for example, Mexico.[46] Some subject all income of resident individuals to tax, but only the domestic income of companies and other enterprises—for example, Brazil.[47] In others only income of domestic source is taxable—for example, Argentina.[48] Each of three largest Latin American republics has a different jurisdictional tax concept.

Under the Colombian income tax law, domiciled individuals are taxed on their income from both Colombian and foreign sources while nondomiciled individuals[49] and juridical persons,

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[43] Under the constitution of Brazil, each of the three governments—federal, state and municipal—may levy a stamp tax. Const., art. 15 (VI), art. 19 (VI), art. 29 (V).

[44] Gumpel and De Sousa, *op. cit. supra* note 27, at 47.

[45] Although foreign income of individuals is not subject to schedular tax because it is not derived from activities carried on in Brazil, such income is, however, subject to the complementary tax. Gumpel and De Sousa, *op. cit. supra* note 27, at 50.

[46] Gumpel and Margain, Taxation in Mexico 64 (1957).

[47] Gumpel and De Sousa, *op. cit supra* note 27, at 50.

[48] Recently, Argentina agreed to give all tax evaders since 1956 a "break" of 70% to 85% if they would voluntarily pay their taxes. More than 250,000 people took advantage of the compromise. National Observer, December 10, 1962, p. 2, col. 5.

[49] Decree 0270 of February 6, 1953, art. 15 (*Diario Official* of Feb. 25 and March 9, 1953).

whether domiciled or not, are taxed only on income from Colombian sources.[50] In Colombia, an individual is presumed to be domiciled, for tax purposes, if he remains in the country voluntarily and continuously for six months or more in a taxable year.[51] Without reference to the time of stay, the same presumption arises if an individual were to open and personally operate a business establishment. The same exception to the duration-of-stay rule applies if the individual engaged in commerce or industry, acquired real estate, procured public or private employment, or performed analogous acts. Individuals are presumed to be domiciled in Colombia if they maintain their family or their business headquarters in the country even if they themselves are not personally present within its borders.

The source of income rules of Colombia include as domestic source income all income from the purchase or sale, in Colombia, of personal property.[52] Domestic source income also includes income produced by realty located in Colombia; earnings from capital invested in the country; and that which originates by reason of any activity executed within the territory of Colombia such as the rendition of a service, the direction of a business or industry even though the primary source may be foreign and regardless of the place where the payment is certified, such as the salaries which are paid in Colombia or abroad with foreign funds, for services rendered in the country, even though the payor is domiciled abroad and even when the employment contract is signed abroad.

Only two Latin American countries grant by law a foreign tax credit,[53] and only one (Honduras) is party to a tax treaty (with the United States). Hence, any effective enforcement of the tax on foreign-source income by Latin American countries would result in extremely burdensome double taxation. The Latin American has a psychological block to the taxation of foreign-source income, and in 1953 the Cuban delegate to the Fiscal Commission of the United Nations proposed a resolution that capital-exporting countries should refrain from taxing income

[50] Law 78 of Dec. 23, 1935, art. 5 (*Diario Official* of January 3, 1936).
[51] Law 78 of December 23, 1935, art. 4 (*Diario Official* of Jan. 3, 1936).
[52] Decree 818 of April 26, 1936, art. 29 (*Diario Official*, of May 5, 1936).
[53] See the exhaustive and scholarly treatise by Elisabeth A. Owens on the foreign tax credit, Owens, Foreign Tax Credit (1961).

which arose outside of their territories. Recently, a number of resolutions were adopted by bodies of the Organization of American States to the effect that the member states should restrict their taxation only to income having a domestic source as a stimulus to the free flow of investment capital.[54]

By and large, income deductions in Latin American countries are not unlike those provided for by the United States Internal Revenue Code. Personal deductions may tend to be of wider application, sometimes including an unmarried or an unemployed sister of the taxpayer, as well as all dependent ascendants and descendants.[55] As was previously indicated, Latin American taxing systems rarely permit the taxpayer to deduct the amount previously paid in foreign income taxes. While a bad debt may be deducted, you must be able to convince the tax authority that the debt is indeed uncollectible. Salaries paid may be deducted by business firms but such deductions are specifically limited. In Colombia, only 36,000 pesos may be taken for the salary paid to the president of the company. This sum, translated into a free-market equivalent of less than 6,000 dollars will easliy discourage a United States investor.

In Latin America, with few exceptions, mineral deposits are considered to be property of the state regardless of who owns the surface, and deductions for depletion create a taxing problem. The governments, although in most cases willing to grant concessions to individuals and companies for working such deposits, have difficulty in reconciling the state-ownership theory with the view that the concessionaire has a wasting asset for which he may take depletion deductions.[56]

The Latin American derived his initial ideas of the income tax from France, where formerly there was no lumping of income into a common taxable mass. Special rules were made applicable

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[54] Department of Economic and Social Affairs, Secretariat of the Economic Commission for Latin America, United Nations, The Latin American Common Market (1959).

[55] Colombian decree 2317 of September 8, 1953, art. 19 (*Diario Oficial* of Sept. 17, 1953); decree 818 of April 26, 1936, art. 88, 89 (*Diario Oficial* of May 5, 1936).

[56] For an analysis of the corporate and non-corporate characteristics of the various forms of business ventures and their application in the development and production of Latin American oil resources, see Raymond, *Tax Aspects of Joint Ventures and Oil Operations in Latin America,* 4 Institute on Private Investments Abroad 63 (1962).

to each category or schedule of income, and special rates or rate tables were prescribed for each schedule. In order to be taxable income, it had to fall within the definition of a particular schedule. If it did not, then it was not subject to tax.

Any individual may receive types of income falling with several schedules, all of which will be taxable.[57] The taxpayer, however, might be some entity other than the individual himself, such as his wholly-owned enterprise. While we may refer to the taxation of corporate enterprises in Latin America, we must understand that corporations, as such, are taxable because they conduct enterprises engaged in activities defined by the Commercial Code of the country as "commercial."[58] The same rule applies to profits of any enterprise, be it conducted by a partnership or one of the several other forms of business organizations recognized by the Civil Law, or simply by an individual proprietor. Commercial profits, as interpreted in Latin America, normally comprise any gains to which the English term, "business profits," would apply.[59]

Latin American taxes were initially imposed only on one or more types of income. This is still true in some of the republics —for example, Guatemala and Ecuador. Among the types originally taxed were the profits of all enterprises registered under the Commercial Code,[60] which for long years past had already required the keeping of specified books of account. Such books and each page thereof had to be duly registered and stamped by an official, usually the Judge of Commerce. Since the enterprise was normally required to be a member of the local Chamber of Commerce, a semi-official organ in Latin America, the government had available for its revenue agents a register of all taxpayers and records for the enforcement of a tax on profits.

Penalties were imposed by the Commercial Code for incorrect

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[57] Crockett, *Tax Patterns in Latin America*, 15 Nat'l Tax J. 93, 96 (1962).

[58] An outline and bibliography on the tax aspects of organizing international operations is contained in the American Management Association Seminar, June 1961, entitled *Going Abroad: The Profit Opportunities of International Business for the Smaller Company*, published by the U. S. Government Printing Office. An explanation of the "commercial" transaction concept may be found in Gumpel and Margain, Taxation in Mexico 55 (1957).

[59] For taxation in the United Kingdom, see Brudno & Bower, Taxation in the United Kingdom—World Tax Series (1957).

[60] A distinction is made between transactions which are governed by the commercial law *(actos de comercio)* as distinguished from those regulated by the civil law *(actos civiles)*.

books and the validity of transactions, as well as any legal redress, depended upon proper entries having been recorded in these books.[61] A certain evidentiary value is still imputed to the mere book entries, and the government in one republic does not even require the filing of a return. The taxpayer enterprise simply writes the Tax Director that its books show a specified amount of net profit for the preceding year, and encloses a copy of its balance sheet and an abbreviated transcript of its profit and loss account. A revenue agent calls to examine the books, making adjustments by eliminating expenditures that are not deductible, such as the profits taxes paid, personal and family expenses of the owners, if any such appear, salaries exceeding deductible limits set by law, and the like. The tax on the commercial profits of an enterprise is usually computed by a progressive rate table. This progression, which sets a penalty on size, often leads to the division of the enterprise into two or more units for tax saving.[62]

In Brazil, the income tax applies to all individuals, corporations, and other entities which either are residents of Brazil or derive income from Brazilian sources.[63] While the income tax on resident individuals will not be treated in detail in this discussion, it may be briefly stated that it consists of two taxes: a schedular tax (at fixed rates between one per cent and ten per cent) which depends on the type of income, regardless of its amount, and a complementary tax (surtax) on total net income (with steeply graduated rates up to fifty per cent) which depends on the amount of net income only, regardless of the nature of the income.

The taxation of Brazilian resident corporations and other entities such as limited-liability companies, commercial partnerships, and the like, is basically very simple. There are two methods of taxation: (1) by withholding at the source, and (2) by assessment.[64]

Withholding at the source applies to certain types of income,

[61] In some of the Latin American countries customs officials are given a share of the fine levied for technical violations of the regulations, and, therefore, have a personal interest in discovering errors. Heavy fines are levied for slight errors or even for slips of the typewriter.

[62] The multiple entity problem is now under attack by the Commissioner of Interinal Revenue in the United States under his authority to reallocate income. Int. Rev. Code of 1954 § 482.

[63] The Taxation of Business Income from Foreign Operations 110-117 (1958).

[64] Reg. art. 1, as modified by Law No. 2,862, art. 19. Gumpel and De Sousa, Taxation in Brazil 90-91 (1957).

especially income from securities made out to the bearer. Withholding rates have been continuously increased during the past few years, and is also applicable to all income which a nonresident individual or entity of Brazil derives from Brazilian sources.[65] The general withholding rate is twenty per cent, with higher rates applying to interest and dividend income from bearer securities, as already mentioned, and to royalties for which the present rate is twenty-five per cent.

The taxation of Brazilian resident entities by assessment proceeds on the basis of an annual return which is filed not later than April 30 of each year.[66] The differentiation of income according to its source, which is important in the taxation of individuals —such as income from business, income from services, income from capital, and so forth—does not apply to corporations and other entities because of the legal fiction that all income of these entities is business income. In other words, as was previously indicated, all income earned by a corporation is business income because it is earned by a corporation.[67] Taxable income is, in Brazil, by and large, identical with the commercial profit as shown in the books of account, plus and minus certain adjustments for tax purposes.

The common Latin American view of profit computation on goods locally produced and sold abroad, or vice versa, excludes any division of profit between the country of production and that of sale. In the United States, our Internal Revenue Code does require such a division.[68] Other commonly accepted but unlegislated rules in Latin America treat interest as having its source at the residence or principal place of business of the debtor, and, if the debtor is a branch of a foreign enterprise, the "branch" would be the debtor if it contracted the loan and entered it on the books.[69] An exception to this general rule is that

[65] Under the Brazilian Income Tax Regulations, the tax on income of a nonresident which was already subjected to taxation at the source, is withheld only to the extent required to raise the total amount of tax to 20%, the withholding rate generally applied to nonresident individuals.

[66] Nabuco, A Statement of the Laws of Brazil 43 (1955).

[67] The Income Tax Regulations of Brazil contain no definition of gross income of entities or rules on the computation of the cost of goods sold. The amount of gross profits determined primarily from the books of the tax-payer. Gumpel and DeSousa, Taxation in Brazil 131 (1957).

[68] Int. Rev. Code of 1954 § 861-864.

[69] The most complete and exhaustive study on the source of income rules in the United States is contained in Dailey, *The Concept of the Source of Income*, 15 Tax L. Rev. 415 (1960).

interest derived from a loan secured by real estate is always treated as having its source in the country in which the real estate is situated. A source of a dividend is usually the country in which the payor corporation was organized. The source of royalties for the use of trade marks, copyrights, patents and the like and rentals of movable property are usually considered as originating in the country in which they are utilized, but in actual practice they would likely be taxed where the payor enters them on its books, and not elsewhere.[70]

Latin American income tax statutes commonly single out a number of specific industries to which the conventional rules for computing taxable income do not apply. Colombia arbitrarily declares that nonresidents deriving receipts from the rental of motion picture films receive taxable income equal to one-half the amount of such receipts.[71] Foreign transportation companies regularly furnishing service between Colombian and foreign points compute taxable income as an amount which bears the same proportion to the company's total profits from all sources as exists between its gross receipts in Colombia and its total receipts. In the Dominican Republic, the net income of foreign insurance companies is legally presumed to be ten per cent of the gross premiums collected for insuring persons or businesses located in the country. Moreover, communications enterprises are presumed to have taxable income equal to ten per cent of gross receipts.[72]

Perhaps the greatest problem concerning income taxation in Latin America is that of rulings, fines and appeals. As pointed out earlier, many income tax systems in Latin America are of recent vintage. Many problems were not anticipated by the drafters of these statutes, and even at this date guidance on many sophisticated tax problems is not provided. While in most cases rulings can be obtained, they are someties obtained only with considerable delay, and then are frequently unreliable. Most Latin American tax statutes provide procedures for contesting

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[70] As an example of the principle of territoriality in taxation, Venezuela renounces the collection of taxes from residents, nonresident foreigners, as well as from nationals on income produced obroad. For other problems in Venezuela, see Shapiro, *Betancourt's Venezuela*, Commentary, June 1961, p. 479.

[71] Decree 1928 of November 5, 1937 (*Diario Oficial* of December 6, 1937).

[72] Law 3861 of June 26, 1954, art. 9, 12 (*Gaceta Oficial* of June 29, 1954).

claims of the administrative authorities. Procedures are frequently lengthy and coupled with a requirement that the disputed amount be deposited, interest free, during the litigation. Where a contest is permitted without deposit of the disputed amount, an adverse ruling may sometimes result in fines and penalties of some magnitude.

Although some of the Latin American tax systems may be lacking in some of the "sophistication" of our Internal Revenue Code, nearly every Latin American nation today has an income tax law patterned more or less after the United States model, although in no instance do the graduated brackets rise to anywhere near the 91 per cent maximum imposed in the United States.[73] Despite these various systems of taxation, however, Latin America places its faith largely on loans—loans from international organizations, and any other source that can make them, for the large projects for which there is no capital. It has not received much. The World Bank has provided a billion dollars in loans to Latin America since 1947. Most of it went into six countries, and the loans from the Export-Import Bank, exclusive of some rather important stabilization operations, have averaged only a net of 100 million dollars a year in the last decade.[74]

There has been growing concern about our foreign aid program, springing from the uncomfortable feeling that it simply isn't working. However, not all of this failure to show progress can be blamed on poorly directed foreign aid because in many instances the major roadblocks to economic betterment have been erected within the receiving countries themselves.

During 1960 contributions from all the industrial nations (Western Europe, Japan and the United States) added up to eight billion dollars, an amount equal to almost one per cent of the combined Gross National Product of the contributing nations. Yet these contributions have come from a wide range of uncoordinated sources, quite often working at cross purposes. No less an authority than Eugene Black, in his farewell address

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[73] Former President Kennedy, however, had in his last tax message indicated a desire to reduce the United States tax rates in order that there be a 65% maximum effective in 1963.

[74] Brazil alone accounted for 38%, Argentina for 16%, and Mexico 12%. Benton, the Voice of America 54n (1961).

to the World Bank, has labeled this bilateral approach to foreign aid as one of the major sources of difficulty and inefficiency.[75]

There are also problems which arise from government guarantees of credit for capital exports. Often these credits involve an addition to the external debt of the importing country. The industrial nations, on their side, yield to pressures and compete with each other in terms that are uneconomic and unsound. Many of the lesser developed countries already have mortgaged their future to the hilt.[76] Between 1955 and 1961 a group of thirty-four countries, accounting for some seventy per cent of the underdeveloped world, more than doubled its external debt. Yet over the same period, the export earnings of these same countries increased by little more than fifteen per cent.

A completely new approach is now recommended in the creation of a new multinational agency designed to plan and administer economic assistance contributed by all its industrial member countries.[77] Such an agency would be managed by the best talent available from the business and financial communities of the Atlantic Nations and Japan, free of political paint and operating with a minimum of waste and inefficiency. Such an agency would have many advantages over the bilateral approach because its talents would be devoted to selecting and financing only those projects which could contribute the most to the growth and prosperity of the recipient nations.

A single multinational agency would also be far less susceptible to political pressures than are individual governments. Experience of both the International Bank and the International Monetary Fund already bears testimony to this fact.[78] Aid-giving countries could not be played off against each other, and a more rational approach to the allocation of scarce aid funds could be

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[75] The problem of technical assistance in Latin America is described in Glick, The Administration of Technical Assistance (1957) and Rottenberg, How United States Business Firms Promote Technological Progress (1957).

[76] *Challenge in Latin America*—Articles by Salvador de Madariaga and Henry Brandon, Saturday Review, March 25, 1961, p. 14.

[77] For another multilateral policy proposal providing for a repayment tax for confiscated property taken by underdeveloped countries, see Tannenbaum, Ten Keys to Latin America (Knopf) 232-236 (1962).

[78] The role of private enterprise in the development of Latin America and the events and policies leading up to the United States public participation is discussed in Bohan, United States Public and Private Investments in Latin America, 4 Institute on Private Investments Abroad 25 (1962).

adopted. Foreign aid programs would be automatically co-ordinated among the donor countries.

A complete separation can never be accomplished between foreign aid and politics because we must recognize that many countries have historical ties and obligations to certain areas. In addition, there just is not enough capital, technical skills nor managerial ability to care for all of the needs of the developing nations.[79] Because of these shortages, a system of priorities has to be created between the different underdeveloped countries, and priorities usually result in political involvement.

The Atlantic Community nations now all belong to the OECD, the Organization for Economic Cooperation and Development. The OECD has a special Development Assistance Committee made up of ten of its principal members plus Japan. Although this committee has no executive powers, it has been suggested that it could serve as a meeting ground for determining how much economic aid might be made available from each of the participants, as well as how this over-all sum could best be divided among the various developing countries. This World Aid Organization would serve as an executive agency and would be manned by men of high technical competence whose task it would be to determine the true needs for economic aid in each of the developing countries, and then to see that the scarce funds which finally become available would be spent most productively and efficiently.

There are only two models of society for Latin America to look to, the United States and Russia, and, as was aptly put by Salvador de Madariaga, our twenty southern neighbors are now between the eagle and the bear.[80] It may be that neither the United States nor the Soviet model suits her, and, if Cuba's troubles are any indication, Latin America may yet develop her own society out of her own traditions.

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[79] De Lesseps S. Morrison, *Alliance for Progress*, 4 Institute on Private Investments Abroad 55 (1962).

[80] De Madariaga, Latin America Between the Eagle and the Bear (1962).

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